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SUBJECT: ARMENIA'S AMCHAM DISCUSSES CONCERNS WITH AMBASSADOR

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SUMMARY

¶1. (SBU) During their June 15 meeting with the Ambassador, members of the American Chamber of Commerce in Armenia (AMCHAM) discussed taxes and customs, rule of law, and the general business environment in Armenia. AMCHAM members expressed dismay at the GOAM's ineffective tax administration and the ways in which it is attempting to compensate for decreased state revenues amid the mounting economic crisis. One member also warned of an imminent collapse in Armenia's housing market due to spiraling mortgage defaults. Against this gloomy backdrop, however, the AMCHAM members offered solutions to achieve greater transparency and fairness in tax and customs administration, and inquired about the possibility of participation in future meetings of the U.S.-Armenia Joint Economic Task Force (USATF) where they could table their proposals.
END SUMMARY.

Disgruntled with Armenia's Tax System

¶2. (SBU) During a June 15 meeting with Ambassador Yovanovitch, AMCHAM members expressed their concerns with a proposed tax increase under discussion in Armenia's parliament. The bill calls for a five percent increase in income tax, as well as an as-yet-unspecified increase in property tax. Most AMCHAM members did not seem persuaded when First Mortgage Company's David Atanessian said: "I don't think it (the bill) will pass as there is a lot of opposition to the draft law both within the government and the public." Another draft law aims to modify the ratio of tax revenues (increasing income tax while lowering value added taxes) in the budget, which may be a result of pressure by the IMF and World Bank on the GOAM to restructure Armenia's tax revenues.

¶3. (SBU) Some members expressed dismay at another draft law that would embed tax representatives within large businesses to ensure better compliance with tax laws. Even though Armenia Bank's Tigran Jrbashian argued that this will actually help to combat the culture of corruption, other members felt such a strategy would simply be countered by wealthy oligarchs "buying off" their new "tax inspectors." Overall, AMCHAM members said they are very frustrated with a tax system that they find both inequitable and outdated.

Customs: Unfair and Unpredictable

¶4. (SBU) AMCHAM members railed against Armenia's customs regime, calling it a "systemized victimization of honest businesspeople" that is rife with corruption and cronyism. "Only ten percent of all

imported goods go through proper customs procedures, while others (importers) avoid payment of appropriate duties," complained First Mortgage Company's David Atanessian. In addition, AMCHAM members complained that Armenian businesses waste valuable time and resources when they must constantly argue with tax authorities on pro forma issues that should be easily resolved. Members also complained that government over-regulation is strangling their ability to grow, while customs inspectors' lack of skills inhibits equality and efficiency. The issues of customs valuation and reference pricing remain the biggest concerns for importers, as the decisions of customs officials are often arbitrary and ungrounded.

Rule of Law: Porous and Outdated

15. (SBU) AMCHAM members unanimously agreed that ill-enforced or non-enforced rules regarding customs and taxes were hindering business development. Members complained that amidst such a crooked business culture, honesty becomes a disadvantage. Oligarch-owned businesses prosper while small and medium enterprises are being squeezed for additional tax payments. "I'm facing unfair competition," griped Hakob Hakobian from the Tufenkian Heritage Hotels firm, and "my competition is stealing my employees after I have trained them for years, just because they have cash" as a result of getting away with tax evasion. Several members grumbled that the government remains oblivious to the negative impact that unenforced or crooked tax and customs regulations have on business development inside Armenia.

16. (SBU) AMCHAM members claimed that approximately seven well-connected oligarchs currently control the construction industry in Yerevan, and that they operate unhindered in spite of their blatant non-compliance with tax and customs regulations. They also complained that legal processes are complicated by the lack of case law in Armenia's judicial system, and that the rules on the books are not only selectively enforced, but also outdated. "We are still

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using Soviet rules for sanitation and construction inspection," protested Tigran Jrbashian of Ameria Bank. .

Impending Mortgage Crisis

17. (SBU) Gurgen Potikian, CEO of Peak Realty, warned of an imminent collapse in Armenia's housing market this fall due to spiraling defaults on mortgages. The local impact of the economic crisis had left many people unemployed and with no income generation. And because many Armenians had collateralized their real estate prior to the onset of the crisis, they are now facing extreme difficulty in repaying their loans. Unless there is a significant change in home-owners' ability to pay their mortgages, Potikian predicted the housing market would collapse by September. In addition to the default on mortgages, the construction industry in Yerevan has ground to a near halt due to the economic crisis.

Possible Solutions to Improve the Business Culture

18. (SBU) Regarding customs administration, one solution proffered by AMCHAM members would be to encourage more transparency by cracking down on the corrupt practices of customs officials and those who bribe them. Another option could be a policy of "double-checking" customs documentation, and stronger oversight on the business practices of the oligarchs. Some members said the only way to change customs administration would be through litigation against the State Revenues Committee that controls tax and customs administration. In this respect, some members voiced optimism over "The Law of Legal Acts" that goes into force in 2010; the law will oblige the GOAM to report on issues such as competition and anti-corruption. The members thought the law would improve the ability of Armenia's legal system to rule on business disputes.

¶9. (SBU) Andrew Hovannisian, the Deputy Director of the Synopsis IT firm, expressed disappointment that the GOAM has not supported the emergence of Yerevan's "mini-Silicon Valley," and has instead supported the establishment of a techno-park in the city of Gyumri. He recommended that the government focus more on the businesses already present in Armenia. Finally, AMCHAM members agreed that their businesses needed better cooperation in order to realize AMCHAM's goals, and they suggested using the U.S.-Armenia Joint Economic Task Force (USATF) as a forum to raise the concerns of Armenia's business community.

COMMENT

¶10. (SBU) The testimonies of AMCHAM members show just how challenging it is to navigate the labyrinth of Armenia's corrupt and overly bureaucratic business culture. The local impact of the economic crisis intensifies these challenges. We find it disconcerting that while the GOAM perennially complains of a paucity of US investment, it has selective hearing when the AMCHAM, one of Armenia's major business associations, raises legitimate concerns in regular meetings with Cabinet officials. We will continue to impress upon GOAM officials that if they are serious about attracting US investment, they must first reform Armenia's unwelcoming business culture.

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